United States Court of Appeals

for the Second Circuit

APPELLEE'S BRIEF

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In The

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

74-2367

ITT WORLD DIRECTORIES, INC.,

Plaintiff-Appellant,

-against-

CIA. EDITORIAL de LISTAS, S.A. and
EDITORIAL de GUIAS LTB., S.A.,

Defendant-Appellees.

BRIEF FOR DEFENDANT-APPELLEES

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DOCKET NO. 74-2367

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Preliminary Statement

Plaintiff-Appellant, ITT World Directories, Inc. ("ITTWD"), appeals from a judgment entered in this diversity action by the United States District Court for the Southern District of New York on October 8, 1974 dismissing its complaint with prejudice. A bench trial was held before the Honorable John M. Cannella, United States District Judge, on February 13, 1974. The Court reserved decision at the conclusion of the trial and on October 4, 1974 rendered its memorandum decision

and order which constituted findings of fact and conclusions of law in favor of the defendants. Appellant ITTWD contends on this appeal that such judgment should be vacated and that judgment should be entered in its favor.

Questions Presented

1. Did ITTWD prove by a preponderance of the evidence at trial that it had made a "mistaken overpayment" to the defendant Cia. Editorial de Listas, S.A. ("CELSA") in the amount of $353,997?

2. Even assuming that ITTWD had offered proof that it had mistakenly paid more than it had intended to pay, is it entitled, under New York law, to restitution if prior to that payment, and at all times thereafter, the sum paid to it was regarded by CELSA as being the correct amount necessary to fulfill ITTWD's obligations under the acquisition agreement?

Statement of Facts

Appellees submit that this is a frivolous appeal. The principal question which appellant purports to raise is whether, as a matter of New York law,* it was entitled to restitution after having allegedly established at trial "proof of an amount due and an erroneous payment of a larger

* ¶10.1 of the acquisition agreement on which this action was based provides as follows:

> "This Agreement shall be governed by and construed in accordance with the laws of the State of New York." (E - 19) (Page references to the separately bound book of exhibits are preceded by "E".)

amount" A. Br. 2.* This "issue" begs the question inasmuch as the Court below found, specifically, that ITTWD had failed "to adduce <u>any facts</u> establishing that it had paid CELSA by mistake" (150a)** (emphasis added). The Court further found that there was a "total failure to present proof sufficient to establish even a <u>prima facie</u> case" and that this failure was "fatal to plaintiff's claim" (145a).

As appellant correctly points out, many of the relevant facts were stipulated at trial and were entered as findings by the Court in its opinion (see 133a-143a). Appellant's sketchy statement of the facts, however, is inadequate for the purpose of this appeal. Accordingly, a more detailed statement is necessary.

On July 9, 1969 CELSA, a corporation organized under the laws of Panama with its principal office in Brazil, entered into an agreement with ITTWD, a Delaware subsidiary of International Telephone and Telegraph Corporation with its principal office in New York, whereby ITTWD agreed to acquire CELSA's wholly-owned subsidiary, a Portuguese corporation referred to herein as "PLT", which was engaged in the publication of telephone directories in Portugal. ITTWD

* Appellant's brief on appeal is cited as "A. Br.".

**Page references to the appendix are followed by the suffix "a".

also agreed to acquire CELSA's 92.1% interest in a Portuguese printing company, referred to herein as "Bertrand", which was organized under the laws of Portugal as a "quota company". The obligations of CELSA under the acquisition agreement were guaranteed by the defendant Editorial de Guias Ltb., S.A.

The acquisition agreement provided that ITTWD would pay CELSA $5,650,000 for all of the outstanding stock of PLT. It also provided that ITTWD would cause Arthur Andersen & Co. to audit the accounts of PLT and Bertrand as of May 31, 1969 and to deliver two documents to both parties as soon as practicable after the closing:

i) certified balance sheets of PLT and Bertrand as of May 31, 1969; and

ii) "a certificate setting forth the tangible net worth of said companies as of May 31, 1969," computed in accordance with a formula set out in the agreement. (E - 16, ¶3.6)

It was agreed that after the "certificate setting forth the tangible net worth of said companies" was delivered to the parties by Arthur Andersen & Co. an adjusting payment would be made. If the combined tangible net worth of the two companies were positive, ITTWD would pay CELSA the amount of such net worth; if it were negative, CELSA would repay to ITTWD the amount of such deficit.

It was also agreed that the combined tangible net worth of the two companies "as set forth in the aforesaid certificate"* would be final and binding unless within 20 days after receipt of the certificate, CELSA delivered to ITTWD an objection in writing stating the amount by which it believed the tangible net worth of the companies exceeded the amount set forth in Arthur Andersen's certificate. If the matter could not be resolved between the parties by negotiation within 20 days after the receipt of CELSA's objection, it would be submitted for arbitration by a second firm of auditors jointly selected by the parties.

ITTWD engaged Arthur Andersen & Co. to audit the balance sheets of PLT and Bertrand and to deliver "a separate statement of the net worth" of the companies (134a, 135a). It was stipulated at trial, and the Court found, that in September, 1969 Arthur Andersen & Co. delivered its final audit report on the combined balance sheets of PLT and Bertrand as of May 31, 1969. The report was dated August 12, 1969 (E-22, 140a). The evidence established, and the Court found, however, that Arthur Andersen never delivered to CELSA the separate "certificate setting forth the tangible net worth of said companies" which, under the agreements was to constitute the sole basis for determining the obligations of the parties

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* E-16, ¶3.6.

(144a). The only document which Arthur Andersen & Co. ever delivered to CELSA was its report on the combined balance sheets of the two companies. At no place in that report did Arthur Andersen & Co. furnish a figure which represented its opinion on the combined tangible net worth of those companies (100a-101a)*. Instead, Arthur Andersen & Co. noted two exceptions to the combined balance sheets. It excepted to the failure of Bertrand to establish a reserve of 6 million escudos ($180,038) to provide for payments against future profits to certain minority quotaholders of Bertrand for the rest of their lives. Because the Arthur Andersen & Co. accountant on the audit, Mr. Jeremy J. Jerram, did not believe that Bertrand would earn sufficient profits over the lives of the minority quotaholders to make these payments, he felt that a reserve to provide for them was necessary -- despite the fact that several of such quotaholders had life expectancies of 30 years.

Arthur Andersen & Co. also took exception to Bertrand's failure to increase its reserve for depreciation of machinery and equipment by 5 million escudos ($173,969). This exception was based on the fact that Bertrand had not followed a fully consistent depreciation policy with respect to machinery acquired in 1960 and earlier, long before Bertrand had been acquired by CELSA (E-23).

* Contrary to appellant's argument (A. Br. 4), Arthur Andersen & Co. never "arrived at" a figure for the combined tangible net worth of the two companies. It was, of course, precisely such figure which the acquisition agreement contemplated would determine the parties' obligations, subject to the aforementioned arbitration provision, and which Arthur Andersen & Co. failed to deliver.

It was undisputed at trial that Arthur Andersen & Co. noted these exceptions in its report because CELSA disagreed that such reserves, or additions, were necessary in order to present fairly the financial condition of Bertrand as of May 31, 1969. Plaintiff's only witness at trial, Mr. Jerram, testified that CELSA's vice president, Mr. Robert S. Arthur, did not agree that the exceptions were well founded and would not agree to book the suggested reserves or additions (66a, 86a-89a, 104a). It is significant to note here that less than one year previously Arthur Andersen & Co. had completed an audit of the accounts of Bertrand as of August 31, 1968 and had taken no exception to the failure of the company to establish or increase these two reserves. It had nevertheless found that the company's balance sheet (with certain exceptions not here relevant) fairly presented its financial condition as of August 31, 1968 (see Defendant's Exhibit A, E-38). Mr. Jerram conceded at trial, moreover, that a balance sheet could fairly present the financial condition of a company as of a particular date even though it had not been prepared in accordance with principles consistent with those applied in the preparation of financial statements for prior periods (117a).

Although Arthur Andersen & Co. did not deliver the certificate called for by the agreement, it was possible to extract from the report an amount which, in the view of Arthur Andersen & Co., represented the combined tangible net

worth of the two companies. If one deducted from the 14,062,480 escudos, which the companies reported as their combined tangible net worth, the 6,000,000 and the 5,000,000 escudo figures which Arthur Andersen & Co. in its exceptions and footnotes had indicated were necessary, in its view, to establish or increase reserves for Bertrand, it could be concluded that Arthur Andersen & Co. believed the combined tangible net worth of the companies to be approximately 3,000,000 escudos, or $138,224.

It was stipulated that a draft of Arthur Andersen's report was in the hands of ITTWD and CELSA in early September, 1969. The evidence established, moreover, that ITTWD fully understood the import of that report before it made the final payment to CELSA on October 31, 1969 in the amount of $492,221 for the combined tangible net worth of the two companies. It was stipulated, and the Court found, that on September 12, 1969, plaintiff's secretary and general counsel, Victor M. Berger, Esq. (who was in attendance throughout the trial), received a telex from ITT in Lisbon which specifically pointed out that the financial statements which Arthur Andersen was reviewing showed a combined tangible net worth of approximately 14,000,000 escudos, but that there were "to be considered" an addition to the reserve for depreciation of 5,000,000 escudos and a new reserve of 6,000,000 escudos for possible future lifetime payments to Bertrand's minority quotaholders. The combination of the increase in the depreciation reserve and the establishment of the reserve for

minority quotaholders, it was pointed out, would result in a "net net worth of approximately 3,000,000 escudos" (see Memorandum Decision, 147a). Upon receipt of this information, Mr. Berger contacted ITTWD's legal counsel in Lisbon on September 16, 1969 seeking his legal opinion on whether or not the payments to Bertrand's minority quotaholders against future profits could "legally be stopped by us at present time" (see Memorandum Decision, 141a). On the following day, September 17, 1969, Mr. Berger received a reply from ITTWD's Lisbon counsel stating:

> "Problem of Bertrand is very involved and it is not clear whether so called 'payments against future profits' can or not [sic] be legally stopped. As you know, we suggested negotiating rather than entering into legal action." (E-8, ¶19)

On the same day that ITTWD received that equivocal telex in New York City, the principals of both contracting parties, Mr. Arthur on behalf of CELSA and Mr. Ted B. Westfall, Chairman of the Board of ITTWD, met at ITTWD's offices in New York City (see Memorandum Decision, 142a).

On the basis of the foregoing facts, the Court found that plaintiff, through its secretary and general counsel, Victor Berger, Esq. "fully understood and was aware of the contents of the August 12 reports" issued by Arthur Andersen & Co. (Memorandum Decision, 147a). This finding of fact is totally ignored by appellant in its brief. Rather than pointing to any evidence in the record that it had made a mistake in the final payment (of which the record is obviously barren), appellant now adopts an unusual tactic: it "admits

that a mistake was made" and argues (with blatant disregard of the record) that it "can offer no explanation for the obvious misreading of the Arthur Andersen Report" (A. Br. 21).

On October 23, 1969 ITTWD's manager of accounting, Mr. John Morrison, prepared a memorandum for Mr. Berger in which he calculated the amount of the final payment that ITTWD was obligated to make to CELSA under the acquisition agreement. Mr. Morrison pointed out in his memorandum that the "net worth per A.A. report was 14,062,780 escudos" or $492,221. (E-8, ¶21) Appellant consciously elected to call neither Mr. Morrison nor Mr. Berger (nor anyone else in its employ, for that matter) as a witness at trial and thus offered no evidence to support its assertion that both its chief accountant and its general counsel "obviously misread" the Arthur Andersen & Co. report.

Mr. Morrison advised the treasurer's department of ITTWD on October 28, 1969 that ITTWD was obligated to pay CELSA $803,239 (which included the combined net worth payment of $492,221 and other amounts not here relevant) and requested a check to be drawn to CELSA's order in that amount. That check was delivered by ITTWD to CELSA's attorney on October 31, 1969. In acknowledging receipt of the check, CELSA's attorney stated in a letter to ITTWD that the check was accepted as a "partial payment" and that he understood an additional payment would be forthcoming after

a determination had been made of the salvage value of certain Bertrand machinery (Memorandum Decision, 142a-143a).

On February 10, 1970, ITTWD sent to CELSA a recalculation it had made of the purchase price it had paid for Bertrand. This recalculation indicated an overpayment of $24,569 resulting from a mathematical error. (The claim for that sum was adjusted by the parties and was therefore not in issue at trial.) Nothing in that recalculation, however, suggested that ITTWD had in fact made a much larger "mistaken overpayment" in the amount of $353,997.

On July 9, 1970 ITTWD authorized Morgan Guaranty Trust Company of New York ("Morgan") to release and pay over to CELSA one-half of a $900,000 escrow fund which had been established in accordance with the terms of the acquisition agreement. Again, no claim was asserted at that time with regard to any such alleged "mistake" (Memorandum Decision, 143a). It was not until July of 1971, when ITTWD blocked the payment by Morgan of the balance of the escrow fund to CELSA, that a claim of "mistake" was first made and this action ensued.

ARGUMENT

POINT I

APPELLANT OFFERED NO EVIDENCE OF ANY MISTAKE ON ITS PART.

At trial, ITTWD failed to offer a shred of evidence on the basic issue presented by its claim of "mistake", namely, its state of mind at the time that the final payment was

made to CELSA. The Restatement of Contracts defines a "mistake" as "a state of mind that is not in accord with the facts." Restatement of Contracts §500 (1932) (emphasis added). Comment "a" to Section 500 adds that "[w]hen it is said that a man labors under a mistake his mental attitude is referred to." This Restatement view is in accord with the law of New York.

> "It is clear that the term [mistake] signifies an erroneous mental conception which influences a person to act or to omit to act." 37 N.Y. Jur. Mistake, Accident, or Surprise §1 (1964).

The term "mistake" is similarly defined for purposes of an action for restitution.

> "Mistake means a state of mind not in accord with the facts." Restatement of Restitution §6 (1937) (emphasis added).

Comment "b" to Section 6 states that a "mistake is an erroneous belief" (emphasis added).

Appellant's only witness at trial, Jeremy J. Jerram, was employed during the relevant period by Arthur Andersen & Co., not by appellant.* Mr. Jerram did not - and could not - testify to ITTWD's state of mind on October 31, 1969, the date of the alleged overpayment. Instead of producing witnesses who could have testified on this issue at the trial (one of whom, Mr. Berger, was in attendance (71a)), appellant sought to rely solely on inferences which it claims that this Court can and should now draw in its favor.

* Mr. Jerram entered ITT's employ in July, 1971 (55a).

Thus, appellant argues that the amount of the final payment was to be based entirely upon an "opinion" rendered by Arthur Andersen & Co.; that Arthur Andersen's "opinion" was that the applicable net worth figure was 3 million escudos; that ITTWD's payment was based upon a net worth figure of 14 million escudos and that the only possible explanation for this alleged "overpayment" was that it had misread and misunderstood the Arthur Andersen & Co. report. (A. Br. 15)

This chain of suppositions is totally devoid of support in the record. In the first place, as noted above, the acquisition agreement did not provide that CELSA would be bound by "the opinion of Arthur Andersen" as appellant contends (A. Br. 15). The auditors were to deliver certified balance sheets of the companies <u>and</u> a certificate setting forth the combined tangible net worth of the companies as of May 31, 1969. It was the certificate alone which, under the agreement, subject to negotiation between the parties and, ultimately, invocation of the arbitration provision of the agreement, would determine the amount of the final payment. Whereas a report was made by Arthur Andersen & Co. on the combined balance sheets of the companies, no "certificate setting forth the tangible net worth of said companies" was ever delivered to CELSA.

The Court found, moreover, that not only did the report manifest that a substantial dispute existed between CELSA and Arthur Andersen & Co. concerning "the tangible net

worth of said companies", but that the implications of that dispute were clearly not misunderstood by ITTWD. Thus, there is absolutely no basis upon which appellant can ask this Court to accept, on faith alone, a proposition which the Court below rejected, namely, that plaintiff's secretary and general counsel and its manager of accounting did not understand the report of the auditors, whom ITTWD had engaged, and that they authorized the final payment to be made to CELSA while laboring under some fundamental misconception concerning the intent and import of the Arthur Andersen & Co. opinion.

The cases which appellant cites in an attempt to relieve itself of its burden of showing a mistake on its part demonstrate, instead, the necessity of its making just such a showing. Gulf Oil Corp. v. Lone Star Producing Co., 322 F.2d 28 (5th Cir. 1963), was correctly distinguished by the Court below (148a-149a). There the plaintiff pleaded and proved that it had mistakenly paid the defendant $3.15 per barrel of oil when the correct amount, based upon a mathematical subtlety inherent in the pricing formula, was $3.05. The Court of Appeals found that the correct price was $3.05 and that there was "no substantial" contention to the contrary. Although no one from the plaintiff's accounting department was called to testify as to how the mistake was made, the manager of the plaintiff's crude oil supply department did testify to the fact of plaintiff's mistake. 322 F.2d at 32.

Therefore, the Court had no difficulty in concluding that "there was simply no explanation for the overpayments except that they were made by mistake of fact". 322 F.2d at 32.

Here the facts are quite to the contrary. CELSA had consistently maintained that the 5 million and 6 million escudo reserves and additions proposed by Arthur Andersen & Co. were unfounded and that CELSA was entitled to the full tangible net worth of 14 million escudos shown on the combined balance sheets of the two companies. This contention was advanced long <u>before</u> appellant allegedly made its "mistaken overpayment." ITTWD adduced no testimony at trial concerning the existence of a mistake on its part, much less the reasons for such an alleged mistake.

Plaintiff also places much reliance upon <u>Valley Bank of Nevada</u> v. <u>Bank of Commerce</u>, 74 Misc.2d 195, 343 N.Y.S.2d 191, (Civ. Ct. N.Y. Co. 1973), <u>reversed on other grounds</u>, N.Y.L.J. Oct. 30, 1973, p. 2, cols. 1 and 2 (App. T., 1st Dept.). There, a drawee bank had paid out on a forged check and sought reimbursement from the collecting bank. The collecting bank first reimbursed the drawee bank and then sued for a refund on the grounds that its reimbursement had been made by mistake.

The Court found that the collecting bank's reimbursement of the drawee bank had, indeed, resulted from a mistake of applicable law, since it was indisputable that the drawee

bank, in those circumstances, had no legal right to reimbursement:

> "The rule of law... firmly accepted in the Uniform Commercial Code - is explicit that a drawee bank that pays an instrument on which the signature of the drawer is forged cannot recover back its payment from a collecting bank that acted in good faith." 74 Misc.2d at 197, 343 N.Y.S.2d at 193 (emphasis added).

In our case it was by no means "firmly accepted" or "explicit" that the reserves or additions suggested by Arthur Andersen & Co. should have been booked and the reported combined tangible net worth of the two companies reduced accordingly.

Likewise, Mutual Life Insurance Company of New York v. Kessler, 25 Misc.2d 242, 202 N.Y.S.2d 92 (Sup. Ct. N.Y. Co. 1960), is of no assistance to plaintiff in attempting to shift its burden of proving its alleged mistake. There, plaintiff had paid out the full death benefits due on one of its life insurance policies without deducting the amount of a loan outstanding against the underlying policy. The defendant admitted the existence of the loan and the fact of overpayment. The Court found that the mistaken payment had been made because of clerical errors committed by four of plaintiff's employees. The issue, therefore, was not whether a mistake had been made and the defendant unjustly enriched thereby, but, rather, whether plaintiff had a legal or equitable remedy available to it. Similarly, in Manufacturers Trust Company v. Diamond, 17 Misc.2d 909, 186 N.Y.S.2d 917, 918 (App. T., 1st Dept. 1959), the plaintiff established that it had committed a mistake, albeit a negligent one.

Appellant also relies on Section 20 of the Restatement of Restitution (A. Br. 9). The underlying assumption of the Section is, however, that there has in fact been established an "excessive" payment arising out of an "erroneous" belief that the payment was necessary for the discharge of a duty. It concludes that the remedy of restitution is available in such circumstances. Here, of course, there was nothing "erroneous" about appellant's belief that CELSA was entitled to the full final payment which was made. As we have demonstrated, inasmuch as Arthur Andersen & Co.'s opinion on the necessity of the two reserves or additions had been vigorously contested by CELSA (a fact which appellant does not and could not deny) the only reasonable explanation for the payment which was made by ITTWD, and accepted by CELSA, was that the amount was agreed upon in accordance with the contractual provision that such disputes were to be negotiated in the first instance.*

The trial Court was entirely correct in finding that:

> "Plaintiff... failed to present to this Court any evidence, either documentary or testimonial, which could be said to support their contention that the payment to CELSA was made under a mistake of fact." (148a, see also 145a).

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* Appellant's theory of "mistake" conveniently ignores the obvious question of why CELSA, after having refused to book the adjustments proposed by Arthur Andersen & Co., would have suddenly and inexplicably agreed to accept a payment which deducted those amounts from the final combined net worth of the two companies.

POINT II

CELSA HAD A CONTRACTUAL RIGHT TO ARBITRATE THIS CONTROVERSY OF WHICH IT WOULD BE PREJUDICIALLY DEPRIVED IF APPELLANT'S BELATED CONTENTION OF UNILATERAL "MISTAKE" WERE NOW ACCEPTED.

Appellant argues that its unilateral view of the acquisition agreement and the "mistake" it claims to have made should be imposed on CELSA on the ground that CELSA has suffered no "change of position" as a result of that alleged "mistake" (A. Br. 10). This analysis, again, ignores the unambiguous terms of the agreement. The Court below found that, if Arthur Andersen & Co. had delivered a "certificate" setting forth a combined tangible net worth of the companies of only $138,224, and if ITTWD had tendered that amount to CELSA in fulfillment of its obligations, CELSA would have had the right under the agreement, which it "would have exercised" (146a), to resort to arbitration to contest such certificate before a second firm of auditors.*

In such an arbitration certain arguments would have been advanced by CELSA with respect to the merits of Arthur Andersen & Co.'s position. The Court below agreed, moreover, that CELSA's dispute with the auditors was "<u>bona fide</u>" (147a). These arguments (which would have been advanced by CELSA in any such arbitration) may be briefly summarized as follows:

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* Appellant appears to suggest that CELSA somehow waived its right to arbitrate (A. Br. 3). This argument is specious. Inasmuch as Arthur Andersen & Co. never delivered the certificate called for by the agreement and ITTWD in fact paid the full amount which CELSA deemed due and owing to it, there was obviously no reason for CELSA to invoke the arbitration clause of the contract.

A. The Proposed Five Million Escudo Increase To The Reserve For Depreciation

1. Acceptance of this recommendation would have resulted in a large increase in a reserve for depreciation of equipment which had been acquired by Bertrand approximately 10 years earlier and prior to Bertrand's acquisition by CELSA. It concededly had little to do with whether Bertrand's financial condition was fairly stated as of May 31, 1969.

2. The only reason for the proposed increase in this reserve was to make the depreciation "consistent" over the life of that equipment (64a, 78a, 116a). Inasmuch as Arthur Andersen & Co. had not been asked to compare the balance sheet of May 31, 1969 with those of prior years to enable it to render an opinion on whether consistent accounting principles had been applied in prior years, there was no reason why such a strict consistency was either necessary or relevant. Plaintiff's only witness, Mr. Jerram, conceded that a balance sheet as of May 31, 1969 could fairly present the financial condition of a company even if it had been prepared on the basis of principles inconsistent with those applied in the preparation of financial statements for prior periods (117a).

3. Arthur Andersen & Co. had audited Bertrand as of August 31, 1968, only 10 months earlier, and had not taken exception to the company's failure to increase the depreciation reserve at that time (74a). Furthermore, Arthur Andersen &

Co. had never altered or withdrawn its opinion on the 1968 balance sheet (79a).

4. The book value of the equipment understated, rather than overstated, its true value. ITTWD recognized this fact and, as a result, agreed to pay CELSA an additional amount for the salvage value of machinery which had been fully depreciated and for which no value was shown on the company's books as of May 31, 1969 (Memorandum Decision, 143a).

B. The Proposed Six Million Escudo Reserve For Payments To Minority Quotaholders

1. The theory behind this reserve was unprecedented. There was no more reason to establish a reserve for advances to be paid on future profits than there would have been for a company to reserve for future rental payments on a long term lease or for future interest payments on its long term debt.

2. The proposed reserve was based upon Mr. Jerram's unsupported conjecture that Bertrand would be unprofitable for the lives of the minority quotaholders, two of whom had life expectancies of 30 years (86a-87a). ITTWD itself, however, expected Bertrand to turn a profit in the first year after its acquisition (E-46). Jerram admitted he had been unaware of ITTWD's profit projection (89a), which, of course, was fully consistent with ITTWD's decision to acquire the company in the first place.

3. Arthur Andersen & Co. had not excepted to the lack of a reserve for payments to the minority quotaholders when it performed its prior audit as of August 31, 1968 (74a).

Judge Cannella remarked in the course of a discussion of the proposed reserve for minority quotaholders:

> "These are the very matters that would have arisen in the arbitration had the arbitration been held" (87a).

In short, appellant seeks to impose upon CELSA ITTWD's unilateral contention as to the proper figure for the combined tangible net worth of the companies and to deprive CELSA of its right under the acquisition agreement to a timely arbitration <u>before</u> the final payment was made.

The argument that CELSA can show no "change of position" as a result of appellant's alleged "mistake" is obviously erroneous. This Court has always regarded the right to arbitrate as an important and substantial right. In <u>Kavit</u> v. <u>A. L. Stamm & Co.</u>, 491 F.2d 1176 (2d Cir. 1974), for example, this Court held that a federal court should decline to exercise its pendent jurisdiction over state law claims when a party has a contractual right to arbitrate those claims:

> "An even greater degree of circumspection is demanded when, as here, exercise of pendent jurisdiction over a state claim will result in the claim being tried to a court rather than to arbitrators. In such cases the federal court normally should stay the trial of the state claims or dismiss them in the absence of any other ground of federal jurisdiction, if properly requested to do so, even when the federal claims cannot be disposed of without a trial. While exceptional circumstances might justify a contrary course, at the moment we cannot think of any." 491 F.2d at 1180.

This emphasis on the importance of the right to arbitrate is consistent with a recent expression of the views of the Supreme Court on the subject. In Scherk v. Alberto Culver Co., 417 U.S. 506 (1974), involving, incidentally, a dispute arising out of an international contract for the sale of a business, the Supreme Court enforced an arbitration clause in the acquisition agreement despite the defendant's claim that the facts involved violations of the securities laws and thus were within the Wilko v. Swan exception to arbitration of claims under the Federal Arbitration Act, 9 U.S.C.A. §1, et seq.

In conclusion on this point, CELSA had substantial grounds for its disagreement with the two net worth deductions proposed by Arthur Andersen, and it also had a right to arbitrate that dispute. The trial Court was correct in concluding that, had full payment not been made,

> "CELSA would have exercised its right to object to the audit figures which in turn could have necessitated a resort to arbitration as provided in the acquisition agreement. The testimony suggests the possibility that there was a bona fide dispute between the parties as to the actual combined tangible net worth of the two acquired companies, and that ITTWD's payment was the result of a conscious device rather than a mistake of oversight." (Memorandum Decision, 146-147a)

POINT III

EVEN IF APPELLANT HAD OFFERED PROOF THAT IT HAD MADE A "MISTAKE" IN CONNECTION WITH ITS PAYMENT ON OCTOBER 31, 1969, SUCH A UNILATERAL MISTAKE WOULD NOT ENTITLE ITTWD TO RELIEF AGAINST CELSA.

Appellant conceded at trial that any mistake it claimed to have made was strictly unilateral (125a). The Court below agreed, stating during the trial:

> "It is a unilateral mistake. There has been no showing of fraud, there has been no showing of coercion, there has been no showing of the awareness on the part of the defendant that there was a mistake in the mind of plaintiff" (125a).

The Court went on to say:

> "I mean, the point is, there is nothing that you did on the part of the defendant which lent anything to the mistake that was made by the plaintiff. All the things that happened here were done by the plaintiff all by himself without any help at all from the defendant" (126a).

The Court's comments accurately summarized the applicable law. Even assuming plaintiff had proved the far-fetched unilateral "mistake" which it belatedly claimed to have made, it would not be entitled to restitution of its alleged "erroneous overpayment". This Court stated the rule in Eastern Freight Ways, Inc. v. United States, 257 F.2d 703, 707 (2d Cir. 1958), in language similar to that used by the Trial Court:

> "Reformation for unilateral mistake is proper only where the mistake is, or should be, known to the other party to the contract, or where it is induced by that party. Restatement of Contracts (1932) §§503-505; 5 Williston on Contracts (Rev. ed. 1937) §§1548, 1573, 1578, 1597."

Inasmuch as CELSA's disagreement with Arthur Andersen & Co.'s views was known and understood by ITTWD several months before the final payment was made, it would be absurd to argue that CELSA knew or should have known that ITTWD was operating under a "mistake" when, in making the final payment for the tangible net worth of the companies, it did not deduct $353,997 from the amount which CELSA had all along maintained was the correct amount. Indeed, plaintiff has never advanced such a claim nor has it ever asserted that CELSA "induced" the alleged "overpayment".

The Restatement of Contracts states the rule as follows:

> "A mistake of only one party that forms the basis on which he enters into a transaction does not of itself render the transaction voidable; nor do such mistakes of both parties if the respective mistakes relate to different matters; but if the mistakes relate to the same matter, the power of avoidance is not precluded because the mistakes of the parties as to that fact are not the same." Restatement of Contracts §503.

This discussion is equally applicable to alleged mistakes committed in the performance of a contract. Section 500(c) provides that "a mistake may arise with reference to the original agreement of the parties or with reference to the performance of a contract."

The application of these principles to the case at bar is clear. On October 31, 1969 ITTWD tendered a sum of money to CELSA in performance of ITTWD's obligations under the acquisition agreement. CELSA accepted that sum in good

faith inasmuch as the sum tendered represented the precise amount which CELSA had consistently contended was the correct figure for the combined tangible net worth of the two companies it was selling. In these circumstances the agreement (or the performance tendered by ITTWD and accepted by CELSA thereunder) is not subject to reformation.

The Restatement conforms with New York law, which, according to ¶10.1 of the acquisition agreement, is controlling in this case (E-19, ¶10.1).

In Van Curler Development Corp. v. City of Schenectady, 59 Misc.2d 621, 627-28, 300 N.Y.S.2d 765, 774 (Sup. Ct. Schenectady Co. 1969), the Court stated the rule as follows:

> "On elementary principles of estoppel a unilateral mistake arising out of one's own neglect does not afford one grounds for relief, especially where the other party relied thereon to his detriment. In other words, one cannot rescind or repudiate a contract, absent fraud, for a mistake which existed in his own mind alone, where each of the parties had equal and adequate means of information, and each exercised his own judgment on the subject matter." (Emphasis added)

The relevant section of the Restatement of Restitution in these circumstances, therefore, is not Section 20, as appellant argues (A. Br. 9), but, rather, Section 12, which provides as follows:

> "A person who confers a benefit upon another, manifesting that he does so as an offer of a bargain which the other accepts or as the acceptance of an offer which the other has made, is not entitled to restitution because of a mistake which the other does not share and the existence of which the other does not know or suspect."

The Restatement provides the following illustration which is pertinent to this appeal:

> "A and B are partners. A makes a computation of the assets of the business which are worth $50,000, but which, by a mathematical error, he finds to be worth $40,000. He adds $10,000 for good will, and offers to sell his share to B for $25,000. B accepts, not knowing or suspecting the basis of the offer or that A has made an error in computation. A is not entitled to restitution." Restatement of Restitution §12, Illustration 3 (1937).

The parallel to the facts of this case is striking. In view of CELSA's disagreement with Arthur Andersen & Co., the amount of the payment for the combined tangible net worth of the two companies became an issue for the parties to negotiate or arbitrate, as the case might have been, pursuant to the terms of the acquisition agreement. Appellant's tender of payment was in the precise amount which CELSA considered its due and was concededly accepted by it in good faith. Even if one were to adopt the unproved assumption that what ITTWD really intended to offer was $138,224, rather than $492,221, its alleged "mistake" in not doing so would afford it no grounds for recovery by way of restitution.

Appellant makes the specious argument, finally, that the District Court somehow "improperly allocated" the parties' respective burdens of proof by imposing upon plaintiff the burden of disproving "defendant's unproven affirmative defenses" (A. Br. 14). This labored argument begs the question by again assuming, contrary to the Court's findings and the evidence adduced at trial, that appellant had established

by a preponderance of such evidence that it had made a "mistaken overpayment". Appellant's references to the affirmative defense of "substituted agreement" which CELSA pleaded in its answer are totally irrelevant. Inasmuch as ITTWD failed to offer a shred of evidence in support of its claimed "mistake", there was no need for CELSA to put on an affirmative defense. Thus, the validity of CELSA's affirmative defenses never became an issue at trial. The only pleadings which were relevant for the purpose of framing the issues for trial were plaintiff's allegations of an "erroneous overpayment" (Complaint ¶ 14,4a) and CELSA's denial of those allegations (Answer ¶ 8, 11a). There was no improper allocation of the burden of proof on that issue. It was appellant's burden to prove its "mistake" by a preponderance of the evidence. It clearly failed to meet that burden.

Conclusion

The judgment of the District Court dismissing the complaint should be affirmed by this Court.

Dated: New York, New York
January 31, 1975

Respectfully submitted,

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